



Western States Petroleum Association  
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**Catherine H. Reheis-Boyd**

Chief Operating Officer and Chief of Staff

May 25, 2007

Mr. Winston Hickox, Chair  
Market Advisory Committee  
Cal/EPA  
1001 I Street  
Sacramento, CA 95812

Dear Winston,

The Western States Petroleum Association (WSPA) is pleased to provide the following comments to the Market Advisory Committee (MAC). WSPA is a non-profit trade association whose members are responsible for the majority of the exploration, production, refining, distribution and marketing of petroleum, natural gas and petroleum products in California and five other western states. As such, the cost-effective implementation of AB 32 is very important to our member companies.

We have re-iterated numerous times in our oral and written statements to the Governor's office, CARB, Cal/EPA, UC scientists and others working on the development and implementation of the AB 32 regulatory program, that WSPA is committed to working cooperatively to achieve the goals of AB 32. Like the MAC, our goal is to see that the provisions of AB 32 are applied in a workable, effective manner, with the least disruption to the state's energy market and with minimal impact to the state's economy.

**WSPA Supports a Market Program**

We understand that achieving the goals of AB 32 will be difficult, complicated and potentially costly. The Congressional Research Service<sup>1</sup> (CRS) quotes potential cost of near \$300 per ton to achieve CO2 reductions in the US via a traditional command and control (no trading) program. In California a \$300/ton cost program could mean costs to the economy of over \$50 billion per year in 2020. On the other hand, the CRS report quotes estimated costs at \$23-\$50 per ton with global trading.

CRS states "...through trading of permits, emissions reductions efforts focus on sources at which controls can be achieved at least cost." CRS also states that for the goal of "achieving a specific level of CO2 reductions ... a tradable permit program may be most appropriate."

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<sup>1</sup> CRS Report for Congress – Climate Change: Design Approaches for a Greenhouse Gas Reductions Program, January 16, 2007.

In California, AB 32 sets a specific goal of reducing statewide CO2 emissions down to 1990 levels by 2020. The Governor has also set a goal of reducing CO2 emissions down to 80% of the 1990 level by 2050.

**WSPA strongly believes that a well-designed Market mechanism, one with high transparency, depth and breadth of trade and low transaction costs, is the best way to achieve the state's GHG reductions goals in the most cost-effective manner.**

### **Cap and Trade Mechanism Is Most Cost-effective, But Not Free**

Although a cap and trade program is the least costly program to achieve specific GHG emission reductions, it is certainly not free. The Congressional Budget Office (CBO) in its April 25, 2007 Economic and Budget Issue Brief – Trade-offs in Allocating Allowances for CO2 Emissions clearly states that, “A cap on U.S. carbon dioxide emissions would impose costs on the economy...” Further, the CBO concludes that “Consumers would likely bear most of the cost burden ... in the form of higher prices.”

We urge the MAC to recommend a cap and trade program that is simple to implement (to keep administrative costs low), provides a high degree of long-term certainty (so that companies can appropriately consider investments to reduce greenhouse gas emissions) and that can link with other trading systems (to minimize volatility in the price of emission allowances).

### **Minimize Auction**

As the CRS and CBO reports describe, there are many possible options in the design of a cap and trade program. We understand that the MAC is evaluating some of these design elements, with considerable focus on auctioning emissions allowances. As the CRS and CBO reports describe, some researchers believe that auctioning the CO2 allowances could lower the emission's cap total cost to the economy, if the revenue were used in ways to mitigate the impact of the cap, such as by lowering taxes.

On the other hand, the CBO is not at all convinced that auctioning CO2 allowances will guarantee lower economy-wide impacts, even if the revenues were used to cut taxes. WSPA does not believe that California politics will allow the “efficient” recycling of the revenue generated by the auctioning of CO2 allowances. Without the efficient recycling of auction revenue, the cost benefits of an auction would be lost. We urge the MAC to recommend a minimum use of auctions.

### **Auction is a Tax**

AB 32 authorizes the Air Resources Board to impose fees that reflect the direct burden on CARB to carry out the program as stated in Speaker Nunez's August 31, 2006 Letter to the Journal. An auction of CO2 emissions allowances that generates revenue beyond CARB's costs is a tax. WSPA believes that an auction is a tax not authorized by AB 32.

### **An Auction Will Disadvantage California Businesses**

An auction would impose a potentially substantial new cost on the California businesses forced to participate in the auction – in essence, it requires them to pay an unknowable amount “up front” for the right to continue to operate during some set period. The need to pay up front as well as the uncertainty of the prices in a potential auction will likely drive investments and jobs out of state.

This uncertainty and its impact on the cost of the GHG allowances to be auctioned will be exacerbated during the first auction cycle due to California business's unfamiliarity with such a far-reaching and novel auction system. The potential effects of this uncertainty on the economy could be similar to the impact that uncertainty had on the price and availability of electricity during California's attempt to deregulate electric power.

In addition, an auction will divert capital away from facilities and operations that must make reductions. The cost of an auction is a one-for-one reduction in the capital available for investment in greenhouse gas reducing projects.

Summarizing, WSPA strongly supports a market program to achieve the state's greenhouse gas reduction goals, but only if it is well designed and minimizes the use of auctions. WSPA is committed to working with CARB and all stakeholders to design the best market program that can achieve the state's goals at the least cost.

Thank you for considering our comments. Please feel free to contact me if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Catherine A. Boyle". The signature is fluid and cursive, with the first name "Catherine" being more prominent.

cc: Lawrence H. Goulder, Vice Chair, Market Advisory Committee  
Dale Bryk, Market Advisory Committee  
Dallas Burtraw, Market Advisory Committee  
Eileen Claussen, Market Advisory Committee  
Daniel J. Dudek, Market Advisory Committee  
Paul Ezekiel, Market Advisory Committee  
Stephen E. Koonin, Market Advisory Committee  
Franz T. Litz, Market Advisory Committee  
Joe Nation, Market Advisory Committee  
Martin Nesbit, Market Advisory Committee  
Jonathan Pershing, Market Advisory Committee  
Nancy Sutley, Market Advisory Committee  
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Brian Prusnek, Governor's Office  
David Crane, Governor's Office  
Linda Adams, CalEPA  
Bob Sawyer, CARB  
Dan Skopec, CalEPA

Mike Scheibel, CARB  
Chuck Sulock – CARB  
Joe Sparano, WSPA  
Michael Barr – Pillsbury, Winthrop, Shaw, Pitmann LLP